

## Internal Revenue Service, Treasury

## § 1.509(a)-3

### § 1.508-4 Effective date.

Except as otherwise provided, §§ 1.508-1 through 1.508-3 shall take effect on January 1, 1970.

(Sec. 7805 of the Internal Revenue Code of 1954, 68A Stat. 917; 26 U.S.C. 7805)

[T.D. 7232, 37 FR 28294, Dec. 22, 1972]

### § 1.509(a)-1 Definition of private foundation.

*In general.* Section 509(a) defines the term *private foundation* to mean any domestic or foreign organization described in section 501(c)(3) other than an organization described in section 509(a) (1), (2), (3), or (4). Organizations which fall into the categories excluded from the definition of *private foundation* are generally those which either have broad public support or actively function in a supporting relationship to such organizations. Organizations which test for public safety are also excluded.

[T.D. 7212, 37 FR 21907, Oct. 17, 1972]

### § 1.509(a)-2 Exclusion for certain organizations described in section 170(b)(1)(A).

(a) *General rule.* Organizations described in section 170(b)(1)(A) (other than in clauses (vii) and (viii)) are excluded from the definition of *private foundation* by section 509(a)(1). For the requirements to be met by organizations described in section 170(b)(1)(A) (i) through (vi), see § 1.170A-9 (a) through (e) and paragraph (b) of this section. For purposes of this section, the parenthetical language *other than in clauses (vii) and (viii)* used in section 509(a)(1) means *other than an organization which is described only in clause (vii) or (viii)*. For purposes of this section, an organization may qualify as a section 509(a)(1) organization regardless of the fact that it does not satisfy section 170(c)(2) because:

(1) Its funds are not used within the United States or its possessions, or

(2) It was created or organized other than in, or under the law of, the United States, any State or territory, the District of Columbia, or any possession of the United States.

(b) *Medical research organizations.* In order to qualify under section 509(a)(1) as a medical research organization de-

scribed in section 170(b)(1)(A)(iii), an organization must meet the requirements of section 170(b)(1)(A)(iii) and § 1.170A-9(c)(2), except that, solely for purposes of classification as a section 509(a)(1) organization, such organization need not be committed to spend every contribution for medical research before January 1 of the fifth calendar year which begins after the date such contribution is made.

[T.D. 7212, 37 FR 21907, Oct. 17, 1972]

### § 1.509(a)-3 Broadly, publicly supported organizations.

(a) *In general*—(1) *General rule.* Section 509(a)(2) excludes certain types of broadly, publicly supported organizations from private foundation status. An organization will be excluded under section 509(a)(2) if it meets the one-third support test under section 509(a)(2)(A) and the not-more-than-one-third support test under section 509(a)(2)(B).

(2) *One-third support test.* An organization will meet the one-third support test if it normally (within the meaning of paragraph (c) or paragraph (d) of this section) receives from permitted sources more than one-third of its support in each taxable year from any combination of—

(i) Gifts, grants, contributions, or membership fees; and

(ii) Gross receipts from admissions, sales of merchandise, performance of services, or furnishing of facilities, in an activity that is not an unrelated trade or business (within the meaning of section 513), subject to certain limitations described in paragraph (b) of this section. For purposes of this section, governmental units, organizations described in section 509(a)(1), and persons other than disqualified persons with respect to the organization shall be referred to as permitted sources. For purposes of this section, the amount of support received from the sources described in paragraph (a)(2)(i) of this section and this paragraph (a)(2)(ii) (subject to the limitations referred to in this paragraph (a)(2)) will be referred to as the numerator of the one-third support fraction, and the total amount of support received (as defined in section 509(d)) will be referred to as the denominator of the one-third support

fraction. Section 1.509(a)-3(f) distinguishes gifts and contributions from gross receipts; § 1.509(a)-3(g) distinguishes grants from gross receipts; § 1.509(a)-3(h) defines membership fees; § 1.509(a)-3(i) defines “any bureau or similar agency of a governmental unit”; § 1.509(a)-3(j) describes the treatment of certain indirect forms of support; paragraph (k) of this section describes the method of accounting for support; § 1.509(a)-3(l) describes the treatment of gross receipts from section 513(a)(1), section 513(a)(2), or section 513(a)(3) activities; § 1.509(a)-3(m) distinguishes gross receipts from gross investment income; and § 1.509(a)-3(n) describes transition rules for organizations that received advance rulings that expire on or after June 9, 2008.

(3) *Not-more-than-one-third support test*—(i) *In general.* An organization will meet the not-more-than-one-third support test under section 509(a)(2)(B) if it normally (within the meaning of paragraph (c) or (d) of this section) receives not more than one-third of its support in each taxable year from the sum of its gross investment income (as defined in section 509(e)) and the excess (if any) of the amount of its unrelated business taxable income (as defined in section 512) derived from trades or businesses that were acquired by the organization after June 30, 1975, over the amount of tax imposed on such income by section 511. For purposes of this section the amount of support received from items described in section 509(a)(2)(B) will be referred to as the numerator of the not-more-than-one-third support fraction, and the total amount of support (as defined in section 509(d)) will be referred to as the denominator of the not-more-than-one-third support fraction. For purposes of section 509(a)(2), paragraph (m) of this section distinguishes gross receipts from gross investment income. For purposes of section 509(e), gross investment income includes the items of investment income described in § 1.512(b)-1(a).

(ii) *Trade or business.* For purposes of section 509(a)(2)(B)(ii), a trade or business acquired after June 30, 1975, by an organization shall include, in addition to other trades or businesses:

(A) A trade or business acquired after such date from, or as a result of the

liquidation of, an organization’s subsidiary which is described in section 502 whether or not the subsidiary was held on June 30, 1975.

(B) A new trade or business commenced by an organization after such date.

(iii) *Allocation of deductions between businesses acquired before, and businesses acquired after, June 30, 1975.* Deductions which are allowable under section 512 but are not directly connected to a particular trade or business, such as deductions referred to in paragraphs (10) and (12) of section 512(b), shall be allocated in the proportion that the unrelated trade or business taxable income derived from trades or businesses acquired after June 30, 1975, bears to the organization’s total unrelated business taxable income, both amounts being determined without regard to such deductions.

(iv) *Allocation of tax.* The tax imposed by section 511 shall be allocated in the same proportion as in paragraph (a)(3)(iii) of this section.

(4) *Purposes.* The one-third support test and the not-more-than-one-third support test are designed to insure that an organization which is excluded from private foundation status under section 509(a)(2) is responsive to the general public, rather than to the private interests of a limited number of donors or other persons.

(b) *Limitation on gross receipts*—(1) *General rule.* In computing the amount of support received from gross receipts under section 509(a)(2)(A)(ii) for purposes of the one-third support test of section 509(a)(2)(A), gross receipts from related activities received from any person, or from any bureau or similar agency of a governmental unit, are includible in any taxable year only to the extent that such receipts do not exceed the greater of \$5,000 or 1 percent of the organization’s support in such taxable year.

(2) *Examples.* The application of this paragraph may be illustrated by the examples set forth below. For purposes of these examples, the term *general public* is defined as persons other than disqualified persons and other than persons from whom the foundation receives gross receipts in excess of the

## Internal Revenue Service, Treasury

## § 1.509(a)-3

greater of \$5,000 or 1 percent of its support in any taxable year, and the term *gross receipts* is limited to receipts from activities which are not unrelated trade or business (within the meaning of section 513).

*Example 1.* For the taxable year 1970, X, an organization described in section 501(c)(3), received support of \$10,000 from the following sources:

Bureau M (a governmental bureau from which X received gross receipts for services rendered)	\$25,000
Bureau N (a governmental bureau from which X received gross receipts for services rendered)	25,000
General public (gross receipts for services rendered)	20,000
Gross investment income	15,000
Contributions from individual substantial contributors (defined as disqualified persons under section 4946(a)(2))	15,000
<b>Total support</b>	<b>100,000</b>

Since the \$25,000 received from each bureau amounts to more than the greater of \$5,000 or 1 percent of X's support for 1970 (1% of \$100,000=\$1,000) under section 509(a)(2)(A)(ii), each amount is includible in the numerator of the one-third support fraction only to the extent of \$5,000. Thus, for the taxable year 1970, X received support from sources which are taken into account in meeting the one-third support test of section 509(a)(2)(A) computed as follows:

Bureau M	\$5,000
Bureau N	5,000
General public	20,000
<b>Total</b>	<b>30,000</b>

Therefore, in making the computations required under paragraph (c), (d), or (e) of this section, only \$30,000 is includible in the aggregate numerator and \$100,000 is includible in the aggregate denominator of the support fraction.

*Example 2.* For the taxable year 1970, Y, an organization described in section 501(c)(3), received support of \$600,000 from the following sources:

Bureau O (gross receipts for services rendered)	\$10,000
Bureau P (gross receipts for services rendered)	10,000
General public (gross receipts for services rendered)	150,000
General public (contributions)	40,000
Gross investment income	150,000
Contributions from substantial contributors	240,000
<b>Total support</b>	<b>600,000</b>

Since the \$10,000 received from each bureau amounts to more than the greater of \$5,000 or 1 percent of Y's support for 1970 (1% of \$600,000=\$6,000), each amount is includible in the numerator of the one-third support fraction only to the extent of \$6,000. Thus, for the taxable year 1970, Y received support from sources required to meet the one-third

support test of section 509(a)(2)(A) computed as follows:

Bureau O	\$6,000
Bureau P	6,000
General public (gross receipts)	150,000
General public (contributions)	40,000
<b>Total</b>	<b>202,000</b>

Therefore, in making the computations required under paragraph (c), (d), or (e) of this section, \$202,000 is includible in the aggregate numerator and \$600,000 is includible in the aggregate denominator of the support fraction.

(c) *Normally*—(1) *In general*—(i) *Definition*. The support tests set forth in section 509(a)(2) are to be computed on the basis of the nature of the organization's normal sources of support. An organization will be considered as "normally" receiving one third of its support from any combination of gifts, grants, contributions, membership fees, and gross receipts from permitted sources (subject to the limitations described in §1.509(a)-3(b)) and not more than one third of its support from items described in section 509(a)(2)(B) for a taxable year and the taxable year immediately succeeding such year, if, for such taxable year and the four taxable years immediately preceding such taxable year, the aggregate amount of the support received during the applicable period from gifts, grants, contributions, membership fees, and gross receipts from permitted sources (subject to the limitations described in §1.509(a)-3(b)) is more than one third, and the aggregate amount of the support received from items described in section 509(a)(2)(B) is not more than one third, of the total support of the organization for such five-year period. A publicly supported organization described under section 509(a)(2) that has failed to meet either the one-third support test of paragraph (a)(2) of this section or the not-more-than-one-third support test of paragraph (a)(3) of this section for two consecutive years will be treated as a private foundation as of the first day of the second consecutive taxable year only for purposes of sections 507, 4940, and 6033. Such an organization must file a Form 990-PF, "Return of Private Foundation or Section 4947(a)(1) Nonexempt Charitable Trust Treated as a Private Foundation," and will be liable for the net investment

tax imposed by section 4940 and, if applicable, the private foundation termination tax imposed by section 507(c), for that second consecutive failed year. For the succeeding years, the organization will be treated as a private foundation for all purposes.

(ii) *First five years of an organization's existence.* See paragraph (d)(1) of this section for the definition of "normally" for organizations in the first five years of their existence.

(2) *Terminations under section 507(b)(1)(B).* For the special rules applicable to the term normally as applied to private foundations that elect to terminate their private foundation status pursuant to the 60-month procedure provided in section 507(b)(1)(B), see the regulations under such section.

(3) *Exclusion of unusual grants.* For purposes of applying the tests for support set forth in paragraphs (a)(2) and (a)(3) of this section, one or more contributions may be excluded from the numerator of the one-third support fraction and from the denominator of both the one-third support and not-more-than-one-third support fractions only if such a contribution meets the requirements of this paragraph (c)(3). The exclusion provided by this paragraph (c)(3) is generally intended to apply to substantial contributions and bequests from disinterested parties, which contributions or bequests—

(i) Are attracted by reason of the publicly supported nature of the organization;

(ii) Are unusual or unexpected with respect to the amount thereof; and

(iii) Would by reason of their size, adversely affect the status of the organization as normally meeting the one-third support test for any of the applicable periods described in this paragraph (c) or paragraph (d) of this section. In the case of a grant (as defined in § 1.509(a)-3(g)) that meets the requirements of this paragraph (c)(3), if the terms of the granting instrument require that the funds be paid to the recipient organization over a period of years, the grant amounts may be excluded for such year or years in which they would otherwise be includible in computing support under the method of accounting on the basis of which the organization regularly computes its in-

come in keeping its books under section 446. However, no item described in section 509(a)(2)(B) may be excluded under this paragraph (c)(3). The provisions of this paragraph (c)(3) shall apply to exclude unusual grants made during any of the applicable periods described in this paragraph (c) or paragraph (d) of this section. See paragraph (c)(5) of this section as to reliance by a grantee organization upon an unusual grant ruling under this paragraph (c)(3).

(4) *Determining factors.* In determining whether a particular contribution may be excluded under paragraph (c)(3) of this section, all pertinent facts and circumstances will be taken into consideration. No single factor will necessarily be determinative. Among the factors to be considered are—

(i) Whether the contribution was made by any person (or persons standing in a relationship to such person which is described in section 4946(a)(1)(C) through 4946(a)(1)(G)) who created the organization, previously contributed a substantial part of its support or endowment, or stood in a position of authority, such as a foundation manager (within the meaning of section 4946(b)), with respect to the organization. A contribution made by a person other than those persons described in this paragraph (c)(4)(i) will ordinarily be given more favorable consideration than a contribution made by a person described in this paragraph (c)(4)(i);

(ii) Whether the contribution was a bequest or an inter vivos transfer. A bequest will ordinarily be given more favorable consideration than an inter vivos transfer;

(iii) Whether the contribution was in the form of cash, readily marketable securities, or assets which further the exempt purposes of the organization, such as a gift of a painting to a museum;

(iv) Except in the case of a new organization, whether, prior to the receipt of the particular contribution, the organization has carried on an actual program of public solicitation and exempt activities and has been able to attract a significant amount of public support;

Internal Revenue Service, Treasury

§ 1.509(a)-3

(v) Whether the organization may reasonably be expected to attract a significant amount of public support subsequent to the particular contribution. In this connection, continued reliance on unusual grants to fund an organization's current operating expenses (as opposed to providing new endowment funds) may be evidence that the organization cannot reasonably be expected to attract future support from the general public;

(vi) Whether, prior to the year in which the particular contribution was received, the organization met the one-third support test described in paragraph (a)(2) of this section without the benefit of any exclusions of unusual grants pursuant to paragraph (c)(3) of this section;

(vii) Whether neither the contributor nor any person standing in a relationship to such contributor which is described in section 4946(a)(1)(C) through 4946(a)(1)(G) continues directly or indirectly to exercise control over the organization;

(viii) Whether the organization has a representative governing body as described in § 1.509(a)-3(d)(3)(i); and

(ix) Whether material restrictions or conditions (within the meaning of § 1.507-2(a)(7)) have been imposed by the transferor upon the transferee in connection with such transfer.

(5) *Grantors and contributors.* Prior to the making of any grant or contribution expected to meet the requirements for exclusion under paragraph (c)(3) of this section, a potential grantee organization may request a determination whether such grant or contribution may be so excluded. Requests for such

determination may be filed by the grantee organization in the time and manner specified by revenue procedure or other guidance published in the Internal Revenue Bulletin. The issuance of such determination will be at the sole discretion of the Commissioner. The organization must submit all information necessary to make a determination of the applicability of paragraph (c)(3) of this section, including all information relating to the factors described in paragraph (c)(4) of this section. If a favorable determination is issued, such determination may be relied upon by the grantor or contributor of the particular contribution in question for purposes of sections 170, 507, 545(b)(2), 642(c), 4942, 4945, 4966, 2055, 2106(a)(2), and 2522 and by the grantee organization for purposes of paragraph (c)(3) of this section.

(6) *Examples.* The application of the principles set forth in this paragraph is illustrated by the examples as follows. For purposes of these examples, the term *general public* is defined as persons other than disqualified persons and other than persons from whom the foundation received gross receipts in excess of the greater of \$5,000 or 1 percent of its support in any taxable year, the term *gross investment income* is as defined in section 509(e), and the term *gross receipts* is limited to receipts from activities which are not unrelated trades or businesses (within the meaning of section 513).

*Example 1.* (i) For the years 2008 through 2012, X, an organization exempt under section 501(c)(3) that makes scholarship grants to needy students of a particular city, received support from the following sources:

2008:	
Gross receipts (general public) .....	\$35,000
Contributions (substantial contributors) .....	36,000
Gross investment income .....	29,000
Total support .....	100,000
2009:	
Gross receipts (general public) .....	34,000
Contributions (substantial contributors) .....	35,000
Gross investment income .....	31,000
Total support .....	100,000
2010:	
Gross receipts (general public) .....	35,000
Contributions (substantial contributors) .....	30,000

	Gross investment income .....	35,000
	Total support .....	100,000
2011:		
	Gross receipts (general public) .....	33,000
	Contributions (substantial contributors) .....	32,000
	Gross investment income .....	35,000
	Total support .....	100,000
2012:		
	Gross receipts (general public) .....	31,000
	Contributions (substantial contributors) .....	39,000
	Gross investment income .....	30,000
	Total support .....	100,000

(ii) In applying section 509(a)(2) to the taxable year 2012, on the basis of paragraph (c)(1)(i) of this section, the total amount of support from gross receipts from the general public (\$168,000) for the period 2008 through 2012, was more than one third, and the total amount of support from gross investment income (\$160,000) was less than one third, of X's total support for the same period (\$500,000). For the taxable years 2012 and 2013, X is therefore considered normally to receive more than one third of its support from the public sources described in section 509(a)(2)(A) and less than one third of its support from items described in section 509(a)(2)(B). The fact that X received less than one third of its support from section 509(a)(2)(A) sources in 2012 and more than one third of its support from items described in section 509(a)(2)(B) in 2011 does not affect its status because it normally met the applicable tests over a five-year period.

*Example 2.* Assume the same facts as in *Example 1* except that in 2012, X also received an unexpected bequest of \$50,000 from A, an elderly widow who was interested in encouraging the work of X, but had no other relationship to it. Solely by reason of the bequest, A became a disqualified person. X used the bequest to create five new scholarships. Its operations otherwise remained the same. Under these circumstances, if A's bequest is included in X's support calculation, X could not meet the five-year support test because the total amount received from gross receipts from the general public (\$168,000) would not be more than one-third of its total support for the five-year period (\$550,000). Because A is a disqualified person, her bequest cannot be included in the numerator of the one-third support test under section 509(a)(2)(A). However, based on the factors set forth in paragraph (c)(4) of this section, A's bequest may be excluded as an unusual grant under paragraph (c)(3) of this section. Therefore, X will be considered to have met the support test for the taxable years 2012 and 2013.

*Example 3.* Y, an organization described in section 501(c)(3), was created by A, the holder of all the common stock in M corporation; B, A's wife; and C, A's business associate. The purpose of Y was to sponsor and equip athletic teams for underprivileged children in the community. Each of the three creators makes small cash contributions to Y. A, B, and C have been active participants in the affairs of Y since its creation. Y regularly raises small amounts of contributions through fundraising drives and selling admission to some of the sponsored sporting events. The operations of Y are carried out on a small scale, usually being restricted to the sponsorship of two to four baseball teams of underprivileged children. In 2009, M recapitalizes and creates a first and second class of 6 percent nonvoting preferred stock, most of which is held by A and B. In 2010, A contributes 49 percent of his common stock in M to Y. A's contribution of M's common stock was substantial and constitutes 90 percent of Y's total support for 2010. A combination of the facts and circumstances described in paragraph (c)(4) of this section preclude A's contribution of M's common stock in 2010 from being excluded as an unusual grant under paragraph (c)(3) of this section for purposes of determining whether Y meets the one-third support test under section 509(a)(2).

*Example 4.* (i) M is organized in 2009 to promote the appreciation of ballet in a particular region of the United States. Its principal activities consist of erecting a theater for the performance of ballet and the organization and operation of a ballet company. M receives a determination letter that it is an organization described in section 501(c)(3) and that it is a public charity described in section 509(a)(2). The governing body of M consists of nine prominent unrelated citizens residing in the region who have either an expertise in ballet or a strong interest in encouraging appreciation of the art form.

(ii) In 2010, Z, a private foundation, proposes to make a grant of \$500,000 in cash to

M to provide sufficient capital for M to commence its activities. Although A, the creator of Z, is one of the nine members of M's governing body, was one of M's original founders, and continues to lend his prestige to M's activities and fund raising efforts, A does not, directly or indirectly, exercise any control over M. M also receives a significant amount of support from a number of smaller contributions and pledges from other members of the general public. M charges admission to the ballet performances to the general public.

(iii) Although the support received in 2010 will not impact M's status as a public charity for its first five taxable years, it will be relevant to the determination of whether M meets the one-third support test under section 509(a)(2) for the 2014 taxable year, using the computation period 2010 through 2014. Within the appropriate timeframe, M may submit a request for a private letter ruling that the \$500,000 contribution from Z qualifies as an unusual grant.

(iv) Under the above circumstances, even though A was a founder and member of the governing body of M, M may exclude Z's contribution of \$500,000 in 2010 as an unusual grant under paragraph (c)(3) of this section for purposes of determining whether M meets the one-third support test under section 509(a)(2) for 2014.

*Example 5.* (i) Assume the same facts as *Example 4(i)* except that, in addition, in 2013, B, a widow, passes away and bequeaths \$4 million to M. During 2009 through 2013, B made small contributions to M, none exceeding \$10,000 in any year. During 2009 through 2013, M received approximately \$450,000 from receipts for admissions and contributions from the general public. At the time of B's death, no person standing in a relationship to B described in section 4946(a)(1)(C) through 4946(a)(1)(G) was a member of M's governing body. B's bequest was in the form of cash and readily marketable securities. The only condition placed upon the bequest was that it be used by M to advance the art of ballet.

(ii) Although the support received in 2013 will not impact M's status as a public charity for its first five taxable years, it will be relevant to the determination of whether M meets the one-third support test under section 509(a)(2) for future years. Within the appropriate timeframe, M may submit a request for a private letter ruling that the \$4 million bequest from B qualifies as an unusual grant.

(iii) Under the above circumstances, M may exclude B's bequest of \$4 million in 2013 as an unusual grant under paragraph (c)(3) of this section for purposes of determining whether M meets the one-third support test under section 509(a)(2) for 2014 and subsequent years.

*Example 6.* (i) N is a research organization that was created by A in 2009 for the purpose

of carrying on economic studies primarily through persons receiving grants from N and engaging in the sale of economic publications. N received a determination letter that it is described in section 501(c)(3) and that it is a public charity described in 509(a)(2). N's five-member governing body consists of A; A's sons, B and C; and two unrelated economists. In 2009, A made a contribution to N of \$100,000 to help establish the organization. During 2009 through 2013, A made annual contributions to N averaging \$20,000 a year. During the same period, N received annual contributions from members of the general public averaging \$15,000 per year and receipts from the sale of its publications averaging \$50,000 per year. In 2013, B made an *inter vivos* contribution to N of \$600,000 in cash and readily marketable securities.

(ii) Although the support received in 2013 will not impact N's status as a public charity for its first five taxable years, it will be relevant to the determination of whether N meets the one-third support test under section 509(a)(2) for future years. In determining whether B's contribution of \$600,000 in 2013 may be excluded as an unusual grant, the support N received in 2009 through 2013 is relevant in considering the factor described in paragraph (c)(4)(vi) of this section, notwithstanding that N received a determination letter that it is described in section 509(a)(2).

(iii) Under the above circumstances, in particular the facts that B is a disqualified person described in section 4946(a)(1)(D) and N does not have a representative governing body as described in paragraphs (c)(4)(viii) and (d)(3)(i) of this section, N cannot exclude B's contribution of \$600,000 in 2013 as an unusual grant under paragraph (c)(3) of this section for purposes of determining whether N meets the one-third support test under section 509(a)(2) for 2014 and future years.

*Example 7.* (i) O is an educational organization created in 2009. O received a determination letter that it is described in section 501(c)(3) and that it is a public charity described in section 509(a)(2). The governing body of O has 9 members, consisting of A, a prominent civic leader, and 8 other unrelated civic leaders and educators in the community, all of whom participated in the creation of O. During 2009 through 2013, the principal source of income for O has been receipts from the sale of its educational periodicals. These sales have amounted to \$200,000 for this period. Small contributions amounting to \$50,000 have also been received during the same period from members of the governing body, including A, as well as other members of the general public.

(ii) In 2013, A contributed \$750,000 of the nonvoting stock of S, a closely held corporation, to O. A retained a substantial portion of the voting stock of S. By a majority vote, the governing body of O decided to retain the S stock for a period of at least five years.

(iii) Although the support received in 2013 will not impact O's status as a public charity for its first five taxable years, it will be relevant to the determination of whether O meets the one-third support test under section 509(a)(2) for future years. In determining whether A's contribution of the S stock in 2013 may be excluded as an unusual grant, the support O received in 2009 through 2013 is relevant in considering the factor described in paragraph (c)(4)(vi) of this section, notwithstanding that O received a determination letter that it is described in section 509(a)(2).

(iv) Under the above circumstances, in particular the facts that A is a foundation manager within the meaning of section 4946(b) and A's contribution is in the form of closely held stock, O cannot exclude A's contribution of the S stock in 2013 as an unusual grant under paragraph (c)(3) of this section for purposes of determining whether O meets the one-third support test under section 509(a)(2) for 2014 and future years.

(d) *Definition of normally; first five years of an organization's existence*—(1) *In general.* An organization will “normally” meet the one-third support test and the not-more-than-one-third support test during its first five taxable years as a section 501(c)(3) organization if the organization can reasonably be expected to meet the requirements of the one-third support test and the not-more-than-one-third support test during that period. With respect to an organization's sixth taxable year, the general definition of normally in paragraph (c)(1) of this section applies. Alternatively, the organization shall be treated as normally meeting the one-third support test and the not-more-than-one-third support test for its sixth taxable year (but not its seventh taxable year) if it meets the one-third support test and the not-more-than-one-third support test under the definition of normally set forth in paragraph (c)(1)(i) of this section for its fifth taxable year (based on support received in its first through fifth taxable years). If a new publicly supported organization described under section 509(a)(2) cannot meet the requirements of the one-third support test or the not-more-than-one-third support test for its sixth taxable year using either the general definition of normally in paragraph (c)(1) of this section or the alternate rule above (effectively failing to meet a public support test for both its fifth and sixth

years), it will be reclassified as a private foundation as of the first day of its sixth taxable year only for purposes of sections 507, 4940, and 6033. Such an organization must file a Form 990-PF, “Return of Private Foundation or Section 4947(a)(1) Nonexempt Charitable Trust Treated as a Private Foundation,” and is liable for the net investment tax imposed by section 4940 and, if applicable, the private foundation termination tax imposed by section 507(c), for its sixth taxable year. Beginning the first day of its seventh taxable year, the organization will be treated as a private foundation for all purposes.

(2) *Basic consideration.* In determining whether an organization can reasonably be expected (within the meaning of paragraph (c)(1)(i) of this section) to meet the one-third support test under section 509(a)(2)(A) and the not-more-than-one-third support test under section 509(a)(2)(B) described in paragraph (a) of this section during its first five taxable years, the basic consideration is whether its organizational structure, current or proposed programs or activities, and actual or intended method of operation are such as to attract the type of broadly based support from the general public, public charities, and governmental units that is necessary to meet such tests. The factors that are relevant to this determination, and the weight accorded to each of them, may differ from case to case, depending on the nature and functions of the organization. An organization cannot reasonably be expected to meet the one-third support test and the not-more-than-one-third support test where the facts indicate that an organization is likely during its first five taxable years to receive less than one-third of its support from permitted sources (subject to the limitations of paragraph (b) of this section) or to receive more than one-third of its support from items described in section 509(a)(2)(B).

(3) *Factors taken into account.* All pertinent facts and circumstances shall be taken into account under paragraph (d)(2) of this section in determining whether the organizational structure, programs or activities, and method of operation of an organization are such



as to enable it to meet the tests under section 509(a)(2) during its first five taxable years. Some of the pertinent factors are:

(i) Whether the organization has or will have a representative governing body which is comprised of public officials, or individuals chosen by public officials acting in their capacity as such; of persons having special knowledge in the particular field or discipline in which the organization is operating; of community leaders, such as elected officials, clergymen, and educators; or, in the case of a membership organization, of individuals elected pursuant to the organization's governing instrument or bylaws by a broadly based membership. This characteristic does not exist if the membership of the organization's governing body is such as to indicate that it represents the personal or private interests of disqualified persons, rather than the interests of the community or the general public.

(ii) Whether a substantial portion of the organization's initial funding is to be provided by the general public, by public charities, or by government grants, rather than by a limited number of grantors or contributors who are disqualified persons with respect to the organization. The fact that the organization plans to limit its activities to a particular community or region or to a special field which can be expected to appeal to a limited number of persons will be taken into consideration in determining whether those persons providing the initial support for the organization are representative of the general public. On the other hand, the subsequent sources of funding which the organization can reasonably expect to receive after it has become established and fully operational will also be taken into account.

(iii) Whether a substantial proportion of the organization's initial funds are placed, or will remain, in an endowment, and whether the investment of such funds is unlikely to result in more than one third of its total support being received from items described in section 509(a)(2)(B).

(iv) In the case of an organization that carries on fundraising activities, whether the organization has developed

a concrete plan for solicitation of funds from the general public on a community or area-wide basis; whether any steps have been taken to implement such plan; whether any firm commitments of financial or other support have been made to the organization by civic, religious, charitable, or similar groups within the community; and whether the organization has made any commitments to, or established any working relationships with, those organizations or classes of persons intended as the future recipients of its funds.

(v) In the case of an organization that carries on community services, such as combating community deterioration in an economically depressed area that has suffered a major loss of population and jobs, whether the organization has a concrete program to carry out its work in the community; whether any steps have been taken to implement that program; whether it will receive any part of its funds from a public charity or governmental agency to which it is in some way held accountable as a condition of the grant or contribution; and whether it has enlisted the sponsorship or support of other civic or community leaders involved in community service programs similar to those of the organization.

(vi) In the case of an organization that carries on educational or other exempt activities for, or on behalf of, members, whether the solicitation for dues-paying members is designed to enroll a substantial number of persons in the community, area, profession, or field of special interest (depending on the size of the area and the nature of the organization's activities); whether membership dues for individual (rather than institutional) members have been fixed at rates designed to make membership available to a broad cross-section of the public rather than to restrict membership to a limited number of persons; and whether the activities of the organization will be likely to appeal to persons having some broad common interest or purpose, such as educational activities in the case of alumni associations, musical activities in the case of symphony societies, or civic affairs in the case of parent-teacher associations.

(vii) In the case of an organization that provides goods, services, or facilities, whether the organization is or will be required to make its services, facilities, performances, or products available (regardless of whether a fee is charged) to the general public, public charities, or governmental units, rather than to a limited number of persons or organizations; whether the organization will avoid executing contracts to perform services for a limited number of firms or governmental agencies or bureaus; and whether the service to be provided is one which can be expected to meet a special or general need among a substantial portion of the general public.

(4) *Example.* The application of this paragraph (d) may be illustrated by the following example:

*Example.* (i) Organization X was formed in January 2008 and uses a taxable year ending December 31. After September 9, 2008, and before December 31, 2008, Organization X filed Form 1023 requesting recognition of exemption as an organization described in section 501(c)(3) and in section 509(a)(2). In its application, Organization X established that it can reasonably be expected to operate as a publicly supported organization under paragraph (d) of this section. Subsequently, Organization X received a ruling or determination letter that it is an organization described in sections 501(c)(3) and 509(a)(2) effective as of the date of its formation.

(ii) Organization X is described in section 509(a)(2) for its first five taxable years (for the taxable years ending December 31, 2008, through December 31, 2012).

(iii) Organization X can qualify as a publicly supported organization beginning with the taxable year ending December 31, 2013, if Organization X can meet the requirements of either § 1.170A-9(f)(2) or § 1.170A-9(f)(3) or paragraphs (a) and (b) of this section for the taxable years ending December 31, 2009, through December 31, 2013, or for the taxable years ending December 31, 2008, through December 31, 2012.

(e) *Determinations on foundation classification and reliance*—(1) A ruling or determination letter that an organization is described in section 509(a)(2) may be issued to an organization. Such determination may be made in conjunction with the recognition of the organization's tax-exempt status or at such other time as the organization believes it is described in section 509(a)(2). The ruling or determination

letter that the organization is described in section 509(a)(2) may be revoked if, upon examination, the organization has not met the requirements of this section. The ruling or determination letter that the organization is described in section 509(a)(2) also may be revoked if the organization's application for a ruling or determination contained one or more material misstatements or omissions of fact or such application was part of a scheme or plan to avoid or evade any provision of the Code. The revocation of the determination that an organization is described in section 509(a)(2) does not preclude revocation of the determination that the organization is described in section 501(c)(3).

(2) *Status of grantors or contributors.*

(i) For purposes of sections 170, 507, 545(b)(2), 642(c), 4942, 4945, 4966, 2055, 2106(a)(2), and 2522, grantors and contributors may rely upon a determination letter or ruling that an organization is described in section 509(a)(2) until the IRS publishes notice of a change of status (for example, in the Internal Revenue Bulletin or Publication 78, "Cumulative List of Organizations described in Section 170(c) of the Internal Revenue Code of 1986," which can be searched at <http://www.irs.gov>). For this purpose, grantors or contributors may also rely on an advance ruling that expires on or after June 9, 2008. However, a grantor or contributor may not rely on such an advance ruling or any determination letter or ruling if the grantor or contributor was responsible for, or aware of, the act or failure to act that resulted in the organization's loss of classification under section 509(a)(2) or acquired knowledge that the IRS had given notice to such organization that it would be deleted from such classification.

(ii) A grantor or contributor (other than one of the organization's founders, creators, or foundation managers (within the meaning of section 4946(b))) will not be considered to be responsible for, or aware of, the act or failure to act that resulted in the loss of the organization's publicly supported classification under section 509(a)(2) if such grantor or contributor has made such grant or contribution in reliance upon

a written statement by the grantee organization that such grant or contribution will not result in the loss of such organization's classification as not a private foundation under section 509(a). Such statement must be signed by a responsible officer of the grantee organization and must set forth sufficient information, including a summary of the pertinent financial data for the five taxable years immediately preceding the current taxable year, to assure a reasonably prudent person that his grant or contribution will not result in the loss of the grantee organization's classification as a publicly supported organization under section 509(a). If a reasonable doubt exists as to the effect of such grant or contribution, or if the grantor or contributor is one of the organization's founders, creators, or foundation managers, the procedure for requesting a determination letter set forth in paragraph (c)(5) of this section may be followed by the grantee organization for the protection of the grantor or contributor.

(3) *Examples.* The provisions of this paragraph (e) may be illustrated by the following examples:

*Example 1.* Y, a calendar year organization described in section 501(c)(3), is created in February 2008 for the purpose of displaying African art. On its exemption application Y shows, under penalties of perjury, that it can reasonably, in accordance with the requirements of paragraph (d) of this section, expect to receive support from the public in 2008 through 2012 that will satisfy the one-third support and not-more-than-one-third support tests described in section 509(a)(2) for its first five taxable years, 2008 through 2012. Y may therefore receive a determination that it meets the requirements of paragraph (a) of this section for its first five taxable years (2008, 2009, 2010, 2011, and 2012), regardless of the public support Y in fact receives during this period.

*Example 2.* Z, a calendar year organization described in section 501(c)(3), is created in July 2008. On its exemption application Z shows, under penalties of perjury, that it can reasonably, in accordance with the requirements of paragraph (d) of this section, expect to receive support from the public in 2008 through 2012 that will satisfy the one-third support and not-more-than-one-third support tests described in section 509(a)(2) for its first five taxable years, 2008 through 2012. Z receives a determination that it is described in section 509(a)(2). However, the support actually received from the public over Z's first five taxable years (2008 through 2012) does

not satisfy the one-third support and not-more-than-one-third support tests described in section 509(a)(2). Moreover, the support Z receives from 2009 through 2013, also does not meet the one-third support and not-more-than-one-third support tests described in section 509(a)(2). Z is described in section 509(a)(2) during its first five years for all purposes. However, because Z has not met the requirements of paragraph (a) of this section for either 2008 through 2012 or 2009 through 2013, Z is not described in section 509(a)(2) for its taxable year 2013. If Z is not described in section 509(a)(1), section 509(a)(3), or section 509(a)(4), then Z will be reclassified as a private foundation as of the first day of 2013. However, for 2013, Z will be treated as a private foundation only for purposes of sections 507, 4940 and 6033. Z must file Form 990-PF and will be liable for the net investment tax imposed by section 4940 and, if applicable, the private foundation termination tax imposed by section 507(c) for 2013. For 2014 and succeeding years, Z will be treated as a private foundation for all purposes (except as provided in paragraph (e)(2) of this section with respect to grantors and contributors).

(f) *Gifts and contributions distinguished from gross receipts*—(1) *In general.* In determining whether an organization normally receives more than one-third of its support from permitted sources, all *gifts* and *contributions* (within the meaning of section 509(a)(2)(A)(i)) received from permitted sources, are includible in the numerator of the support fraction in each taxable year. However, *gross receipts* (within the meaning of section 509(a)(2)(A)(ii)) from admissions, sales of merchandise, performance of services, or furnishing of facilities, in an activity which is not an unrelated trade or business, are includible in the numerator of the support fraction in any taxable year only to the extent that such gross receipts do not exceed the limitation with respect to the greater of \$5,000 or 1 percent of support which is describing paragraph (b) of this section. The terms *gifts* and *contributions* shall, for purposes of section 509(a)(2), have the same meaning as such terms have under section 170(c) and also include bequests, legacies, devises, and transfers within the meaning of section 2055 or 2106(a)(2). Thus, for purposes of section 509(a)(2)(A), any payment of money or transfer of property without adequate consideration shall be considered a *gift* or *contribution*. Where payment is made or property transferred

## § 1.509(a)-3

## 26 CFR Ch. I (4-1-13 Edition)

as consideration for admissions, sales of merchandise, performance of services, or furnishing of facilities to the donor, the status of the payment or transfer under section 170(c) shall determine whether and to what extent such payment or transfer constitutes a *gift* or *contribution* under section 509(a)(2)(A)(i) as distinguished from *gross receipts* from related activities under section 509(a)(2)(A)(ii). For purposes of section 509(a)(2), the term *contributions* includes qualified sponsorship payments (as defined in § 1.513-4) in the form of money or property (but not services).

(2) *Valuation of property.* For purposes of section 509(a)(2), the amount includible in computing support with respect to gifts, grants or contributions of property or use of such property shall be the fair market or rental value of such property at the date of such gift or contribution.

(3) *Examples.* The provisions of this paragraph (f) may be illustrated by the following examples:

*Example 1.* P is a local agricultural club described in section 501(c)(3). In order to encourage interest and proficiency by young people in farming and raising livestock, it makes awards at its annual fair for outstanding specimens of produce and livestock. Most of these awards are cash or other property donated by local businessmen. When the awards are made, the donors are given recognition for their donations by being identified as the donor of the award. The recognition given to donors is merely incidental to the making of the award to worthy youngsters. For these reasons, the donations will constitute *contributions* for purposes of section 509(a)(2)(A)(i). The amount includible in computing support with respect to such contributions is equal to the cash contributed or the fair market value of other property on the dates contributed.

*Example 2.* Q, a performing arts center, enters into a contract with a large company to be the exclusive sponsor of the center's theatrical events. The company makes a payment of cash and products in the amount of \$100,000 to Q, and in return, Q agrees to make a broadcast announcement thanking the company before each show and to provide \$2,000 of advertising in the show's program (2% of \$100,000 is \$2,000). The announcement constitutes use or acknowledgment pursuant to section 513(i)(2). Because the value of the advertising does not exceed 2% of the total payment, the entire \$100,000 is a qualified sponsorship payment under section 513(i),

and \$100,000 is treated as a contribution for purposes of section 509(a)(2)(A)(i).

*Example 3.* R, a charity, enters into a contract with a law firm to be the exclusive sponsor of the charity's outreach program. Instead of making a cash payment, the law firm agrees to perform \$100,000 of legal services for the charity. In return, R agrees to acknowledge the law firm in all its informational materials. The total fair market value of the legal services, or \$100,000, is a qualified sponsorship payment under section 513(i), but no amount is treated as a contribution under section 509(a)(2)(A)(i) because the contribution is of services.

(g) *Grants distinguished from gross receipts*—(1) *In general.* In determining whether an organization normally receives more than one-third of its support from public sources, all *grants* (within the meaning of section 509(a)(2)(A)(i)) received from permitted sources are includible in full in the numerator of the support fraction in each taxable year. However, *gross receipts* (within the meaning of section 509(a)(2)(A)(ii)) from admissions, sales of merchandise, performance of services, or furnishing of facilities, in an activity which is not an unrelated trade or business, are includible in the numerator of the support fraction in any taxable year only to the extent that such gross receipts do not exceed the limitation with respect to the greater of \$5,000 or 1 percent of support which is described in paragraph (b) of this section. A grant is normally made to encourage the grantee organization to carry on certain programs or activities in furtherance of its exempt purposes. It may contain certain terms and conditions imposed by the grantor to insure that the grantee's programs or activities are conducted in a manner compatible with the grantor's own programs and policies and beneficial to the public. The grantee may also perform a service or produce a work product which incidentally benefits the grantor. Because of the imposition of terms and conditions, the frequent similarity of public purposes of grantor and grantee, and the possibility of benefit resulting to the grantor, amounts received as grants for the carrying on of exempt activities are sometimes difficult to distinguish from amounts received as gross receipts from the carrying on of exempt activities.

The fact that the agreement, pursuant to which payment is made, is designated a *contract* or a *grant* is not controlling for purposes of classifying the payment under section 509(a)(2).

(2) *Distinguishing factors.* For purposes of section 509(a)(2)(A)(ii), in distinguishing the term *gross receipts* from the term *grants*, the term *gross receipts* means amounts received from an activity which is not an unrelated trade or business, if a specific service, facility, or product is provided to serve the direct and immediate needs of the payor, rather than primarily to confer a direct benefit upon the general public. In general, payments made primarily to enable the payor to realize or receive some economic or physical benefit as a result of the service, facility, or product obtained will be treated as *gross receipts* with respect to the payee. The fact that a profitmaking organization would, primarily for its own economic or physical betterment, contract with a nonprofit organization for the rendition of a comparable service, facility or product from such organization constitutes evidence that any payments received by the nonprofit payee organization (whether from a governmental unit, a nonprofit or a profitmaking organization) for such services, facilities or products are primarily for the economic or physical benefit of the payor and would therefore be considered *gross receipts*, rather than *grants* with respect to the payee organization. For example, if a nonprofit hospital described in section 170(b)(1)(A)(iii) engages an exempt research and development organization to develop a more economical system of preparing food for its own patients and personnel, and it can be established that a hospital operated for profit might engage the services of such an organization to perform a similar benefit for its economic betterment, such fact would constitute evidence that the payments received by the research and development organization constitute *gross receipts*, rather than *grants*. Research leading to the development of tangible products for the use or benefit of the payor will generally be treated as a service provided to serve the direct and immediate needs of the payor, while basic research or studies carried on in the physical or

social sciences will generally be treated as primarily to confer a direct benefit upon the general public.

(3) *Examples.* The application of this paragraph may be illustrated by the following examples:

*Example 1.* M, a nonprofit research organization described in section 501(c)(3), engages in some contract research. It receives funds from the government to develop a specific electronic device needed to perfect articles of space equipment. The initiative for the project came solely from the government. Furthermore, the government could have contracted with profitmaking research organizations which carry on similar activities. The funds received from the government for this project are gross receipts and do not constitute *grants* within the meaning of section 509(a)(2)(A)(i). M provided a specific product at the government's request and thus was serving the direct and immediate needs of the payor within the meaning of subparagraph (2) of this paragraph.

*Example 2.* N is a nonprofit educational organization described in section 501(c)(3). Its principal activity is to operate institutes to train employees of various industries in the principles of management and administration. The government pays N to set up a special institute for certain government employees and to train them over a 2-year period. Management training is also provided by profitmaking organizations. The funds received are included as *gross receipts*. The particular services rendered were to serve the direct and immediate needs of the government in the training of its employees within the meaning of subparagraph (2) of this paragraph.

*Example 3.* The Office of Economic Opportunity makes a community action program grant to O, an organization described in section 509(a)(1). O serves as a *delegate agency* of OEO for purposes of financing a local community action program. As part of this program, O signs an agreement with X, an educational and charitable organization described in section 501(c)(3), to carry out a housing program for the benefit of poor families. Pursuant to this agreement, O pays X out of the funds provided by OEO to build or rehabilitate low income housing and to provide advisory services to other nonprofit organizations in order for them to meet similar housing objectives, all on a nonprofit basis. Payments made from O to X constitute *grants* for purposes of section 509(a)(2)(A) because such program is carried on primarily for the direct benefit of the community.

*Example 4.* P is an educational institute described in section 501(c)(3). It carries on studies and seminars to assist institutions of higher learning. It receives funds from the

government to research and develop a program of black studies for institutions of higher learning. The performance of such a service confers a direct benefit upon the public. Because such program is carried on primarily for the direct benefit of the public, the funds are considered a *grant*.

*Example 5.* Q is an organization described in section 501(c)(3) which carries on medical research. Its efforts have primarily been directed toward cancer research. Q sought funds from the government for a particular project being contemplated in connection with its work. In order to encourage its activities, the government gives Q the sum of \$25,000. The research project sponsored by government funds is primarily to provide direct benefit to the general public, rather than to serve the direct and immediate needs of the government. The funds are therefore considered a *grant*.

*Example 6.* R is a public service organization described in section 501(c)(3) and composed of State and local officials involved in public works activities. The Bureau of Solid Waste, Management of the Department of Health, Education, and Welfare paid R to study the feasibility of a particular system for disposal of solid waste. Upon completion of the study, R was required to prepare a final report setting forth its findings and conclusions. Although R is providing the Bureau of Solid Waste Management with a final report, such report is the result of basic research and study in the physical sciences and is primarily to provide direct benefit to the general public by serving to further the general functions of government, rather than a direct and immediate governmental needs. The funds paid to R are therefore a *grant* within the meaning of section 509(a)(2).

*Example 7.* R is the public service organization referred to in example 6. W, a municipality described in section 170(c)(1), decides to construct a sewage disposal plant. W pays R to study a number of possible locations for such plant and to make recommendations to W, based upon a number of factors, as to the best location. W instructed R that in making its recommendation, primary consideration should be given to minimizing the costs of the project to W. Since the study commissioned by W was primarily directed toward producing an economic benefit to W in the form of minimizing the costs of its project, the services rendered are treated as serving W's direct and immediate needs and are includible as *gross receipts* by R.

*Example 8.* S is an organization described in section 501(c)(3). It was organized and is operated to further African development and strengthen understanding between the United States and Africa. To further these purposes, S receives funds from the Agency for International Development and the Department of State under which S is required to carry out the following programs: Selec-

tion, transportation, orientation, counseling, and language training of African students admitted to American institutions of higher learning; payment of tuition, other fees, and maintenance of such students; and operation of schools and vocational training programs in underdeveloped countries for residents of those countries. Since the programs carried on by S are primarily to provide direct benefit to the general public, all of the funds received by S from the Federal agencies are considered *grants* within the meaning of section 509(a)(2).

(h) *Definition of membership fees*—(1) *General rule.* For purposes of section 509(a)(2), the fact that a membership organization provides services, admissions, facilities, or merchandise to its members as part of its overall activities will not, in itself, result in the classification of fees received from members as *gross receipts* rather than *membership fees*. If an organization uses membership fees as a means of selling admissions, merchandise, services, or the use of facilities to members of the general public who have no common goal or interest (other than the desire to purchase such admissions, merchandise, services, or use of facilities), then the income received from such fees shall not constitute *membership fees* under section 509(a)(2)(A)(i), but shall, if from a related activity, constitute *gross receipts* under section 509(a)(2)(A)(ii). On the other hand, to the extent the basic purpose for making the payment is to provide support for the organization rather than to purchase admissions, merchandise, services, or the use of facilities, the income received from such payment shall constitute *membership fees*.

(2) *Examples.* The provisions of this paragraph may be illustrated by the following examples:

*Example 1.* M is a symphony society described in section 501(c)(3). Its primary purpose is to support the local symphony orchestra. The organization has three classes of membership. Contributing members pay annual dues of \$10, sustaining members pay \$25, and honorary members pay \$100. The dues are placed in a maintenance fund which is used to provide financial assistance in underwriting the orchestra's annual deficit. Members have the privilege of purchasing subscriptions to the concerts before they go on sale to the general public, but must pay the same price as any other member of the public. They also are entitled to attend a

## Internal Revenue Service, Treasury

## § 1.509(a)–3

number of rehearsals each season without charge. Under these circumstances, M's receipts from the members constitute *membership fees* for purposes of section 509(a)(2)(A)(i).

*Example 2.* N is a theater association described in section 501(c)(3). Its purpose is to support a repertory company in the community in order to make live theatrical performances available to the public. The organization sponsors six plays each year. Members of the organization are entitled to a season subscription to the plays. The fee paid as dues approximates the retail price of the six plays, less a 10-percent discount. Tickets to each performance are also sold directly to the general public. The organization also holds a series of lectures on the theater which members may attend. Under these circumstances, the fees paid by members as dues will be considered *gross receipts* from a related activity. Although the fees are designated as membership fees, they are actually admissions to a series of plays.

(i) *Bureau defined*—(1) *In general.* The term *any bureau or similar agency of a governmental unit* (within the meaning of section 509(a)(2)(A)(ii)), refers to a specialized operating unit of the executive, judicial, or legislative branch of government where business is conducted under certain rules and regulations. Since the term *bureau* refers to a unit functioning at the operating, as distinct from the policymaking, level of government, it is normally descriptive of a subdivision of a department of government. The term *bureau*, for purposes of section 509(a)(2)(A)(ii), would therefore not usually include those levels of government which are basically policymaking or administrative, such as the office of the Secretary or Assistant Secretary of a department, but would consist of the highest operational level under such policymaking or administrative levels. Each subdivision of a larger unit within the Federal Government, which is headed by a Presidential appointee holding a position at or above Level V of the Executive Schedule under 5 U.S.C. 5316, will normally be considered an administrative or policymaking, rather than an operating, unit. Amounts received from a unit functioning at the policymaking or administrative level of government will be treated as received from one bureau or similar agency of such unit. Units of a governmental agency above the operating level shall be aggregated

and considered a separate bureau for this purpose. Thus, an organization receiving gross receipts from both a policymaking or administrative unit and an operational unit of a department will be treated as receiving gross receipts from two *bureaus* within the meaning of section 509(a)(2)(A)(ii). For purposes of this subparagraph, the Departments of Air Force, Army, and Navy are separate departments and each is considered as having its own policymaking, administrative, and operating units.

(2) *Examples.* The provisions of this paragraph may be illustrated by the following examples:

*Example 1.* The Bureau of Health Insurance is considered a *bureau* within the meaning of section 509(a)(2)(A)(ii). It is a part of the Department of Health, Education, and Welfare, whose Secretary performs a policymaking function, and is under the Social Security Administration, which is basically an administrative unit. The Bureau of Health Insurance is in the first operating level within the Social Security Administration. Similarly, the National Cancer Institute would be considered a *bureau*, as it is an operating part of the National Institutes of Health within the Department of Health, Education, and Welfare.

*Example 2.* The Bureau for Africa and the Bureau for Latin America are considered *bureaus* within the meaning of section 509(a)(2)(A)(ii). Both are separate operating units under the administrator of the Agency for International Development, a policymaking official. If an organization received gross receipts from both of these bureaus, the amount of gross receipts received from each would be subject to the greater of \$5,000 or 1 percent limitation under section 509(a)(2)(A)(ii).

*Example 3.* The Bureau of International Affairs of the Civil Aeronautics Board is considered a *bureau* within the meaning of section 509(a)(2)(A)(ii). It is an operating unit under the administrative office of the Executive Director. The subdivisions of the Bureau of International Affairs are Geographic Areas and Project Development Staff. If an organization received gross receipts from these subdivisions, the total gross receipts from these subdivisions would be considered gross receipts from the same *bureau*, the Bureau of International Affairs, and would be subject to the greater of \$5,000 or 1 percent limitation under section 509(a)(2)(A)(ii).

*Example 4.* The Department of Mental Health, a State agency which is an operational part of State X's Department of Public Health, is considered a *bureau*. The Department of Public Health is basically an administrative agency and the Department of Mental Health is at the first operational level within it.

*Example 5.* The Aeronautical Systems Division of the Air Force Systems Command, and other units on the same level, are considered separate *bureaus* with the meaning of section 509(a)(2)(A)(ii). They are part of the Department of the Air Force which is a separate department for this purpose, as are the Army and Navy. The Secretary and the Under Secretary of the Air Force perform the policy-making function, the Chief of Staff and the Air Force Systems Command are basically administrative, having a comprehensive complement of staff functions to provide administration for the various divisions. The Aeronautical Systems Division and other units on the same level are thus the first operating level, as evidenced by the fact that they are the units that let contracts and perform the various operating functions.

*Example 6.* The Division of Space Nuclear Systems, the Division of Biology and Medicine, and other units on the same level within the Atomic Energy Commission are each separate *bureaus* within the meaning of section 509(a)(2)(A)(ii). The Commissioners (which make up the Commission) are the policymakers. The general manager and the various assistant general managers perform the administrative function. The various divisions perform the operating function as evidenced by the fact that each has separate programs to pursue and contracts specifically for these various programs.

(j) *Grants from public charities*—(1) *General rule.* For purposes of the one-third support test in section 509(a)(2)(A), grants (as defined in paragraph (g) of this section) received from an organization described in section 509(a)(1) (hereinafter referred to in this subparagraph as a *public charity*) are generally includible in full in computing the numerator of the recipient's support fraction of the taxable year in question. It is sometimes necessary to determine whether the recipient of a grant from a public charity has received such support from the public charity as a grant, or whether the recipient has in fact received such support as an indirect contribution from a donor to the public charity. If the amount received is considered a grant from the public charity, it is fully includible in the numerator of the sup-

port fraction under section 509(a)(2)(A). However, if the amount received is considered to be an indirect contribution from one of the public charity's donors which has passed through the public charity to the recipient organization, such amount will retain its character as a contribution from such donor and, if, for example, the donor is a substantial contributor (as defined in section 507(d)(2)) with respect to the ultimate recipient, such amount shall be excluded from the numerator of the support fraction under section 509(a)(2). If a public charity makes both an indirect contribution from its donor and an additional grant to the ultimate recipient, the indirect contribution shall be treated as made first.

(2) *Indirect contributions.* For purposes of subparagraph (1) of this paragraph, an indirect contribution is one which is expressly or impliedly earmarked by the donor as being for, or for the benefit of, a particular recipient (rather than for a particular purpose).

(3) *Examples.* The provisions of this paragraph may be illustrated by the following examples:

*Example 1.* M, a national foundation for the encouragement of the musical arts, is an organization described in section 170(b)(1)(A)(vi). A gives M a donation of \$5,000 without imposing any restrictions or conditions upon the gift. M subsequently makes a \$5,000 grant to X, an organization devoted to giving public performances of chamber music. Since the grant to X is treated as being received from M, it is fully includible in the numerator of X's support fraction for the taxable year of receipt.

*Example 2.* Assume M is the same organization described in example 1. B gives M a donation of \$10,000, but requires that M spend the money for the purpose of supporting organizations devoted to the advancement of contemporary American music. M has complete discretion as to the organizations of the type described to which it will make a grant. M decides to make grants of \$5,000 each to Y and Z, both being organizations described in section 501(c)(3) and devoted to furthering contemporary American music. Since the grants to Y and Z are treated as being received from M, Y and Z may each include one of the \$5,000 grants in the numerator of its support fraction for purposes of section 509(a)(2)(A). Although the donation to M was conditioned upon the use of the funds for a particular purpose, M was free to select the ultimate recipient.



*Example 3.* N is a national foundation for the encouragement of art and is an organization described in section 170(b)(1)(A)(vi). Grants to N are permitted to be earmarked for particular purposes. O, which is an art workshop devoted to training young artists and claiming status under section 509(a)(2), persuades C, a private foundation, to make a grant of \$25,000 to N. C is a disqualified person with respect to O. C made the grant to N with the understanding that N would be bound to make a grant to O in the sum of \$25,000, in addition to a matching grant of N's funds to O in the sum of \$25,000. Only the \$25,000 received directly from N is considered a grant from N. The other \$25,000 is deemed an indirect contribution from C to O and is to be excluded from the numerator of O's support fraction.

(k) *Method of accounting.* For purposes of section 509(a)(2), an organization's support will be determined under the method of accounting on the basis of which the organization regularly computes its income in keeping its books under section 446. For example, if a grantor makes a grant to an organization payable over a term of years, such grant will be includible in the support fraction of the grantee organization under the method of accounting on the basis of which it regularly computes its income in keeping its books under section 446.

(l) *Gross receipts from section 513(a) (1), (2), or (3) activities.* For purposes of section 509(a)(2)(A)(ii), gross receipts from activities described in section 513(a) (1), (2), or (3) will be considered gross receipts from activities which are not unrelated trade or business.

(m) *Gross receipts distinguished from gross investment income.* (1) For purposes of section 509(a)(2), where the charitable purpose of an organization described in section 501(c)(3) is accomplished through the furnishing of facilities for a rental fee or loans to a particular class of persons, such as aged, sick, or needy persons, the support received from such persons will be considered *gross receipts* (within the meaning of section 509(d)(2)) from an activity which is not an unrelated trade or business, rather than *gross investment income*. However, if such organization also furnishes facilities or loans to persons who are not members of such class and such furnishing does not contribute importantly to the accomplishment of such organization's exempt

purposes (aside from the need of such organization for income or funds or the use it makes of the profits derived), the support received from such furnishing will be considered *rents or interest* and therefore will be treated as *gross investment income* within the meaning of section 509(d)(4), unless such income is included in computing the tax imposed by section 511.

(2) The provisions of this paragraph may be illustrated by the following example:

*Example.* X, an organization described in section 501(c)(3), is organized and operated to provide living facilities for needy widows of deceased servicemen. X charges such widows a small rental fee for the use of such facilities. Since X is accomplishing its exempt purpose through the rental of such facilities, the support received from the widows is considered *gross receipts* within the meaning of section 509(d)(2). However, if X rents part of its facilities to persons having no relationship to X's exempt purpose, the support received from such rental will be considered *gross investment income* within the meaning of section 509(d)(4), unless such income is included in computing the tax imposed by section 511.

(n) *Transition rules.* (1) An organization that received an advance ruling, that expires on or after June 9, 2008, that it will be treated as an organization described in section 509(a)(2) will be treated as meeting the requirements of paragraph (d)(1) of this section for the first five taxable years of its existence as a section 501(c)(3) organization unless the IRS issued to the organization a proposed determination prior to September 9, 2008, that the organization is not described in sections 170(b)(1)(A)(vi) and 509(a)(1) or in section 509(a)(2).

(2) Paragraph (d)(1) of this section shall not apply to an organization that received an advance ruling that expired prior to June 9, 2008, and that did not timely file with the IRS the required information to establish that it is an organization described in sections 170(b)(1)(A)(vi) and 509(a)(1) or in section 509(a)(2).

(3) An organization that fails to meet a public support test for its first taxable year beginning on or after January 1, 2008, under the regulations in this section may use the prior test set forth in §§ 1.509(a)-3(a)(2) and 1.509(a)-3(a)(3) or § 1.170A-9(e)(2) or § 1.170A-

## § 1.509(a)-4

## 26 CFR Ch. I (4-1-13 Edition)

9(e)(3) as in effect before September 9, 2008, (as contained in 26 CFR part 1 revised April 1, 2008) to determine whether the organization may be publicly supported for its 2008 taxable year based on its satisfaction of a public support test for taxable year 2007, computed over the period 2003 through 2006.

(4) *Examples.* The application of this paragraph (n) may be illustrated by the following examples:

*Example 1.* (i) Organization M was formed in January 2004, and uses a taxable year ending June 30. Organization M received an advance ruling letter that it is recognized as an organization described in section 501(c)(3) effective as of the date of its formation and that it is treated as a publicly supported organization under section 509(a)(2) during the five-year advance ruling period that will end on June 30, 2008. This date is on or after June 9, 2008.

(ii) Under the transition rule, Organization M is a publicly supported organization described in section 509(a)(2) for the taxable years ending June 30, 2004, through June 30, 2008. Organization M does not need to establish within 90 days after June 30, 2008, that it met a public support test under § 1.170A-9(e) or § 1.509(a)-3, as in effect prior to September 9, 2008, (as contained in 26 CFR part 1 revised April 1, 2008) for its advance ruling period.

(iii) Organization M can qualify as a public charity beginning with the taxable year ending June 30, 2009, if Organization M can meet the requirements of § 1.170A-9(f)(2) or § 1.170A-9(f)(3) or paragraphs (a)(2) and (a)(3) of this section for the taxable years ending June 30, 2005, through June 30, 2009, or for the taxable years ending June 30, 2004, through June 30, 2008. In addition, for its taxable year ending June 30, 2009, Organization M may qualify as a publicly supported organization by availing itself of the transition rule contained in paragraph (n)(iii) of this section, which looks to support received by M in the taxable years ending June 30, 2004, through June 30, 2007.

*Example 2.* (i) Organization N was formed in January 2000 and uses a December 31 taxable year. Organization N received a final determination that it was recognized as tax-exempt under section 501(c)(3) and as a public charity prior to September 9, 2008.

(ii) For taxable year 2008, Organization N will qualify as publicly supported if it meets the requirements under either § 1.170A-9(f)(2) or § 1.170A-9(f)(3) or paragraphs (a)(2) and (a)(3) of this section for the five-year period January 1, 2004, through December 31, 2008. Organization N will also qualify as publicly supported for taxable year 2008 if it meets the requirements under either § 1.170A-9(e)(2) or § 1.170A-9(e)(3) or §§ 1.509(a)-3(a)(2) and

1.509(a)-3(a)(3) as in effect prior to September 9, 2008, (as contained in 26 CFR part 1 revised April 1, 2008) for taxable year 2007, using the four-year period from January 1, 2003, through December 31, 2006.

(o) *Effective/applicability date.* This section shall generally apply to taxable years beginning after December 31, 1969 except paragraphs (a)(2), (a)(3)(i), (c), (d), (e), (k) and (n) of this section shall apply to tax years beginning on or after January 1, 2008. For tax years beginning after December 31, 1969 and beginning before January 1, 2008, §§ 1.509(a)-3(a)(2), 1.509(a)-3(a)(3)(i), 1.509(a)-3(c), 1.509(a)-3(d), 1.509(a)-3(e), and 1.509(a)-3(k) as in effect on December 31, 2007 (as contained in 26 CFR part 1 revised April 1, 2008) shall apply.

[T.D. 7212, 37 FR 21907, Oct. 17, 1972, as amended by T.D. 7784, 46 FR 37889, July 23, 1981; T.D. 8423, 57 FR 33443, July 29, 1992; T.D. 8991, 67 FR 20437, Apr. 25, 2002; T.D. 9423, 73 FR 52549, Sept. 9, 2008; T.D. 9549, 76 FR 55764, Sept. 8, 2011; T.D. 9549, 76 FR 61946, Oct. 6, 2011]

### § 1.509(a)-4 Supporting organizations.

(a) *In general.* (1) Section 509(a)(3) excludes from the definition of *private foundation* those organizations which meet the requirements of subparagraphs (A), (B), and (C) thereof.

(2) Section 509(a)(3)(A) provides that a section 509(a)(3) organization must be organized, and at all times thereafter operated, exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more specified organizations described in section 509(a)(1) or (2). Section 509(a)(3)(A) describes the nature of the support or benefit which a section 509(a)(3) organization must provide to one or more section 509(a)(1) or (2) organizations. For purposes of section 509(a)(3)(A), paragraph (b) of this section generally describes the organizational and operational tests; paragraph (c) of this section describes permissible purposes under the organizational test; paragraph (d) of this section describes the requirement of supporting or benefiting one or more *specified* publicly supported organizations; and paragraph (e) of this section describes permissible beneficiaries and activities under the operational test.